

Unit 6 Economic indicators

Activities: Guidance and answers

Activity 6.1 Price inflation in the UK

- 1** a 1975 b 2001, 2008
- 2** a 1971–1980 b 2001–2010
- 3** Price inflation reduces the amount of goods and services a fixed amount of money can buy over time. That is, inflation rides the purchasing power of money incomes – i.e. their real value falls. If the average price level in the UK in 2010 had increased by a factor of 12 since 1970 then £1 in 1970 would be worth just over 8 pence in 2010.

Activity 6.2 A calculated problem

- 1** Year 3 = \$34.85; Year 4 = \$37.80
- 2** Year 3 = 139.4; Year 4 = 151.2
- 3** 51.2%
- 4** a Year 3 at 16.1% (i.e. $\$34.85/\30); b Year 2 at 7.1% (i.e. $\$30/\28)
- 5**

Changes in the number, structure and composition of households, for example due to inward migration and an ageing population	This will change the 'typical' household and its spending patterns. It will be important to monitor spending patterns across a range of representative households as household structure and composition changes
Changes in retailing, for example online retailing over the Internet	It will be important to expand or amend the sample of retail outlets used to monitor prices so that it includes online retailers
Changes in the quality of goods and services, for example the increased performance and efficiency of cars and household goods such as microwaves and ovens.	This is very difficult to do and is not recommended unless it is possible to monitor changes in product quality relative to changes in prices
New goods and services not previously available, such as 3D flatscreen televisions and iPads	These goods should be included in the 'basket' of goods to monitor prices and spending patterns if consumer spending on these items becomes significant

Activity 6.3 How inflation can affect different households

- 1** Inflation reduces the purchasing power of disposable incomes and therefore reduces the amount of goods and services individuals can buy over time.
- 2** a low income b high income
- 3** People who have borrowed money may be made better off by inflation since it will reduce the real value of the amount they have to repay. People whose incomes rise at the same or a higher rate than inflation will be no worse or even better off.
- 4** a high income earners who have skills that are in demand
b the unemployed, disabled, single parents, long-term sick and old-age pensioners on low fixed incomes

Activity 6.4 Deflating the Celtic Tiger

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% annual change in consumer prices	The percentage by which prices have on average increased year on year for a basket of consumer goods and services purchased by the 'average' household
% annual growth in gross domestic product	The percentage by which the total value of output in the economy has changed year on year
% unemployment rate	The proportion of the total workforce that is willing and able to work but is without paid employment

- 2 The rate of inflation has been relatively low for most of the period rising to no more than around 6% in the year 2000. There was deflation between 2008 and 2010.

The unemployment rate fell from a peak of over 15% in 1993 to around 5% for most of the last decade, but it increased again rapidly to around 12% from 2008 to 2010 during the economic recession.

Growth in output was rapid during second half of the 1990s at between 8% to 11% per year. It slowed during the last decade and fell sharply in 2008, turning negative during the economic recession, i.e. the economy contracted.

- 3 The annual rate of price inflation turned negative indicating that consumer prices had on average fallen in 2009 over 2008 levels. This is shown as the plotted line for the rate of change in consumer prices going below zero by crossing below the horizontal axis.
- 4 In 2009 price inflation became negative. That is, there was deflation. At the same time the rate of unemployment increased sharply and there was negative economic growth. The widespread fall in aggregate demand resulted in many firms losing sales and therefore cutting back their output and labour forces. Firms were forced to cut prices to compete for reduced sales and to sell off stocks of goods that were building up while demand for them was falling.

Activity 6.5 Calculating unemployment rates

	2005	2010
Czech Republic	7.92%	6.66%
France	8.75%	9.07%
Japan	4.42%	5.08%
Mexico	3.51%	5.07%
Spain	9.15%	18.00%
Turkey	9.53%	15.93%
USA	5.04%	9.18%

Activity 6.6 What causes unemployment?

Your report should cover and expand on the following.

Article	Cause of unemployment	Possible actions?
Firms cut output as consumer spending falls	Widespread fall in consumer demand	Expansionary fiscal and monetary policy
Government introduces minimum wage law...	Increase in wage costs reduces demand for labour	Set minimum wage at lower level; subsidize training to improve skills and productivity of low-skilled workers on lowest wages
State council votes to increase unemployment tax	Cost of employing people rises so firms cut their demand for labour; some people may choose to be unemployed because benefits are more generous than wages for some low-paid jobs	Cut unemployment tax; cut unemployment benefits
Business experts call for help for manufacturing industries	Competition from producers overseas, resulting in a fall in demand for domestically produced goods	Impose trade barriers, such as quotas and tariffs, to restrict imports and to raise their prices; subsidize manufacturers to offset their costs so they can lower prices without losing profits
700 jobs lost in switch to new technology	Substitution of labour with old skills by new, advanced machinery and equipment	Provide or subsidize training to teach workers new skills;

Activity 6.7 The multiplier effect

- 1 400
- 2 1,360
- 3 As consumption of electricity falls, power providers may cut their output and workforces.
- 4 Demand for coal and oil will fall. This will reduce the demand for coal miners and oil platform workers.
- 5 The fall in aggregate demand for goods and services will become more widespread.

Activity 6.8 A sorry tale to tell

- 1 If fewer people are in paid employment revenues from income and indirect taxes will fall. At the same time public spending on unemployment and welfare support may rise as more people and families suffer hardship
- 2 The loss of income can cause significant hardship. This can also result in arguments and the break-up of families.
- 3 Unemployed people and their families may suffer health problems as their diets are affected because they are unable to afford enough of the right types of food. A loss of self-esteem among unemployed people may also result in them drinking more heavily or even taking drugs. Some unemployed may even become so desperate that they commit suicide.

4 Your letters might cover the following issues.

A teenager living with parents who are unemployed	Unsure if he or she will find a job; the longer the teenager spends unemployed the more unemployable he or she might become; the teenager cannot afford to help pay towards costs of running the parents' home; he or she cannot afford to go out with friends and enjoy a social life
An unemployed person in his or her early thirties with children to support	Worried about being able to support his or her family; if he or she has a large mortgage, worried about losing his or her home
A person in his or her late fifties who until recently has been in work all his or her life	Anxious that his or her skills are out of date and that he or she is too old ever to get another job; possibly too proud to claim unemployment assistance

Activity 6.9 Really growing?

- 1 Qatar
- 2 Portugal
- 3 Zimbabwe

Activity 6.10 Boom or bust?

- 1 The economic cycle refers to the recurrent pattern of fairly predictable fluctuations in the growth rate of real GDP around its long-run trend rate of growth.
- 2 Both countries appear to experience an economic cycle in the rate of growth in their real output or GDP. Periods of relatively healthy annual growth have been followed by slower and even negative growth when the size of their economies, in terms of their output and income, has shrunk. For example, both countries experienced an economic recession towards the end of the last decade, as did many other economies.
- 3 Economic growth rates peaked in both countries during the mid-1990s and again in the middle of the following decade. Real output expanded annually by more than 4% in most years during the 1990s in Malta. Growth was particularly strong in South Africa in the last decade with annual growth rates above 4% from 2004 to 2008.
- 4 Economic growth slowed considerably and turned negative, indicating economic recession, in Malta in 2001 and again in 2008 and 2009. In South Africa economic growth was negative at the start of the 1990s and again at the end of the last decade.
- 5 During an economic downturn and recession consumer expenditure, investment, employment and government revenues are all likely to be falling. As consumer spending falls firms will experience an increase in their stocks of unsold goods and falling revenues. They will cut their output and employment in response. They will also push back any investment plans they have until there are clear signs of recovery. Government revenues from direct and indirect taxes will fall as unemployment rises, firms profits fall and spending on goods and services contracts.

Activity 6.11 Economic boom, environmental bust

- 1** Economic growth is a sustained increase in the real value or output of an economy, measured by the increase in GDP, expenditure or income adjusted for rising prices.
- 2** 8% per year
- 3** The benefits for Chinese people of the economic growth are likely to have been increased income and living standards, plus more employment opportunities and goods and services to enjoy.
- 4** The article suggests the fast pace of growth is not sustainable because of the environmental damage and pollution it is causing. This is also harming food production and causing health problems.
- 5** Social and environmental costs are related to increasing health problems, devastation due to flooding, the build up of waste, polluted water supplies, the loss of usable farmland, the loss of species and reduced biodiversity.
- 6** Your discussions may have covered the following points.
 - If the Chinese government invests more of its own spending on environmental protection measures then public spending on other projects, including the wages of public sector workers, may have to fall or taxes may have to rise.
 - Increasing the price of natural resources such as wood, water, oil and coal, will increase the costs of producing many other goods and services and push up prices for consumers. The profits of many private sector firms may also be squeezed, resulting in cost cutting measures which may include reduced investment and cuts in their workforces.
 - Complying with regulations increases burdens on business.